

**Letter of Findings: 09-0710  
Sales and Use Tax  
For the Years 2006, 2007, 2008**

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**ISSUES**

**I. Sales Tax – Imposition.**

**Authority:** IC § 6-2.5-2-1; IC § 6-2.5-8-8; IC § 6-2.5-4-1; IC § 6-8.1-5-1; [45 IAC 2.2-8-12](#); Lafayette Square Amoco, Inc. v. Indiana Dep't of Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007).

Taxpayer protests the assessment of sales tax on some items.

**II. Use Tax – Imposition.**

**Authority:** IC § 6-8.1-5-1; IC § 6-8.1-5-4; IC § 6-2.5-4-1; IC § 6-2.5-8-8; Lafayette Square Amoco, Inc. v. Indiana Dep't of Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007).

Taxpayer protests the assessment of use tax on some items.

**III. Tax Administration – Negligence Penalty.**

**Authority:** IC § 6-8.1-10-2.1; [45 IAC 15-11-2](#).

Taxpayer protests the imposition of the ten percent negligence penalty.

**STATEMENT OF FACTS**

Taxpayer is an Indiana sole proprietorship. Taxpayer's business is comprised of three different activities: public transportation within and outside of Indiana, retail sales of equipment locally – including rental of equipment to customers - and over the Internet, and lastly excavation contractor work primarily in Indiana with a few jobs in Kentucky. The majority of the excavation work is performed as a service with small sales of materials on a time-and-materials basis. Taxpayer reports his income on schedule C for federal purposes and files a joint Indiana return with his spouse.

The Indiana Department of Revenue ("Department") conducted a sales and use tax audit of Taxpayer for the years 2006, 2007, and 2008, which resulted in the assessment of additional sales and use tax, negligence penalty, and interest. Taxpayer protested a number of audit items. A hearing was held and this Letter of Findings ensues. Because Taxpayer protested numerous items, this Letter of Findings will address the issues in as efficient a manner as possible but also giving clear guidance to Taxpayer and the Department as to the Letter's findings. Additional facts will be provided as necessary.

**I. Sales Tax – Imposition.**

**DISCUSSION**

The Department notes that all tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(b), (c); Lafayette Square Amoco, Inc. v. Indiana Dep't of Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

After the audit, Taxpayer presented protested items in groupings organized by audit report page number (the audit report is dated May 15, 2009). For each audit report page that contained protested items, Taxpayer listed the line item it was protesting and the reason for the protest and attached to each group the documentation it was presenting to the Department for those particular items. This section of the Letter of Findings will refer to the page number and line item in stating the Department's final determination on the matter.

Page 9, line 2: The Department assessed sales tax on what Taxpayer claimed was a sale of a backhoe to an Illinois customer over the Internet. Taxpayer, however, as a favor to its customer, delivered the backhoe to a location in Indiana where the backhoe was painted before its final destination in Illinois. The Department's position is that Taxpayer is considered to have delivered the backhoe in Indiana and therefore should have collected Indiana sales tax on the transaction. IC § 6-2.5-4-1 states in relevant part:

- (a) A person is a retail merchant making a retail transaction when he engages in selling at retail.
- (b) A person is engaged in selling at retail when, in the ordinary course of his regularly conducted trade or business, he:
  - (1) acquires tangible personal property for the purpose of resale; and
  - (2) transfers that property to another person for consideration.
- (c) For purposes of determining what constitutes selling at retail, it does not matter whether:
  - (1) the property is transferred in the same form as when it was acquired;
  - (2) the property is transferred alone or in conjunction with other property or services; or
  - (3) the property is transferred conditionally or otherwise.
- (d) Notwithstanding subsection (b), a person is not selling at retail if he is making a wholesale sale as described in section 2 of this chapter.

(e) The gross retail income received from selling at retail is only taxable under this article to the extent that the income represents:

- (1) the price of the property transferred, without the rendition of any service; and
- (2) except as provided in subsection (g), any bona fide charges which are made for preparation, fabrication, alteration, modification, finishing, completion, delivery, or other service performed in respect to the property transferred before its transfer and which are separately stated on the transferor's records.

For purposes of this subsection, a transfer is considered to have occurred after delivery of the property to the purchaser.

(Emphasis added).

Taxpayer's protest of this item on Page 9, line 2, is denied.

Page 9, line 4; Page 9, line 29; Page 15, line 14: The Department's audit made an adjustment for materials sold on a time-and-material basis on which no sales tax was charged or collected. In most cases Taxpayer paid sales tax at the time of purchase on the materials that were being resold in retail transactions. Sales tax was assessed on a presumed 10 percent markup of the materials sold. Taxpayer no longer protests this methodology, however Taxpayer points to these line items as including tax on a portion of the invoices that were for hauling or excavating services. Taxpayer is correct, no sales tax should be assessed on the portion of the invoices that is a service. A supplemental audit will reduce the sales tax assessed on the transactions accordingly. IC § 6-2.5-4-1(e).

Page 9, line 6: Taxpayer protests this item on the basis that the customer was exempt, however, Taxpayer did not have an exemption certificate available. Taxpayer presented evidence that it sent letters to its customer requesting that a certificate be presented and asks the Department for leniency pending receipt of the certificate. As of the date of this Letter of Findings Taxpayer has not presented the exemption certificate, therefore the assessment of tax on this transaction remains. IC § 6-2.5-2-1(b); IC § 6-2.5-8-8(a); [45 IAC 2.2-8-12\(b\)](#).

Page 15, line 1: Taxpayer now presents an exemption certificate for this item. A supplemental audit will remove this item from assessment of sales tax. IC § 6-2.5-8-8(a).

Page 15, line 4: Taxpayer states that the amount listed on this invoice for stone was for hauling, the stone itself was paid for by the customer directly to the provider of the stone directly. However, the invoice Taxpayer presents is from Taxpayer to the customer and lists each type of stone along with quantities with relevant charges in addition to the separate charge for hauling. Taxpayer has not presented any evidence that shows that it was not paid for the stone; however, if the hauling charges were included in the audit assessment of sales tax, that amount should be subtracted from the assessed total. IC § 6-2.5-4-1(e).

Page 20, line 1: Taxpayer contends that this line item is the same as those on Page 16, lines 7, 8, 9, 10 and it is therefore being double-taxed on these items. Taxpayer presents an invoice no. 1652 that does not match the customer identified on the referenced lines on Page 16. The invoice also does not list any number in the "total" line of the invoice. Taxpayer has not met its burden to show that the Department's assessment of tax on this item is incorrect.

### FINDING

Taxpayer's protest of the assessment of sales tax is denied in part and sustained in part as delineated above.

## II. Use Tax – Imposition.

### DISCUSSION

The Department notes again that all tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(b), (c); *Lafayette Square Amoco, Inc. v. Indiana Dep't of Revenue*, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

The Department's audit review of Taxpayer's purchase invoices revealed additional taxable purchases on which no sales or use tax had been paid. Taxable purchases include diesel fuel, equipment repair parts, equipment rentals, equipment purchases, construction materials, tires, office supplies, and other taxable purchases. Taxpayer protested some of these items. After the audit, Taxpayer presented protested items in groupings organized by audit report page number (the audit report is dated May 15, 2009). For each audit report page that contained protested items, Taxpayer listed the line item it was protesting and the reason for the protest and attached to each group the documentation it was presenting to the Department for those particular items. This section of the Letter of Findings will refer to the page number and line item in stating the Department's final determination on the matter.

Page 11, lines 1, 2, and 3: Taxpayer purchased construction materials on which no sales or use tax was paid. Taxpayer claimed that these materials were used on exempt construction projects. The Department's audit could not readily establish that these items were used on specific exempt projects and also could not determine if they were used on lump sum jobs or time-and-material jobs. As a result the Department's audit taxed these items at cost and treated them as lump sum materials. After the hearing Taxpayer presented invoices for the purchases as well as billings to clients who are in all likelihood exempt. However, Taxpayer was unable to correlate the invoices and the billings to demonstrate that the purchases would have been exempt.

Page 11, lines 13, 14, 16, 18, 19, 20, 21, 22, 23, 24, 25, and 30; Page 12, lines 1, 2, 3, 4, 5, 6, 7, 8, 16, 17, 18, 19, 20, 22, 23, 24, 26, 27, and 29; Page 13, lines 4, 5, 6, 7, 8, 10, 11, 12, 13, 14, 15, 16, 17, 18, 19, 20, 21, 22, 23,

24, 25, 26, and 27; Page 16, lines 2, 3, 4, 5, 6, 7, 10, 11, 12, 13, **14**, 16, 18, 22, 24, 25, and 26; Page 17, lines 1, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 26, 28, 30, 31, and 32; Page 18, lines 6, 7, 8, and 9; Page 21, lines **4**, 7, 8, 9, 10, and 15; Page 24, lines 5, 6, 9, 10, 11, 12, 13, 14, 15, 16, 22, 23, 24, and 27; Page 25, lines 1, 7, 9, 10, 11, 12, 13, 14, 15, 16, 17, 18, 19, 20, 21, **22, 23, 24, 25, 26, 27, 28, 29, 30, 31**, and **32**: (the bolded line numbers related to diesel purchases): The Department found that Taxpayer had taxable purchases of diesel fuel (off road), equipment repair parts, tires, small tools and equipment rentals on which tax had not been paid. Upon reviewing Taxpayer's accounts payable records, the Department's audit found that a number of the invoices were not available for review because while Taxpayer had copies of monthly statements from vendors, it did not retain the invoices.

The Department's auditor determined that since Taxpayer performed distinct business activities, the purchases of diesel fuel would be treated in the following manner: diesel fuel was considered taxable when the fuel was indicated to be dyed (off road) and considered to be used by Taxpayer in their excavating business. Diesel fuel purchased for "on road" use was considered exempt as being used by Taxpayer in the public transportation portion of their business. However, where invoices were missing and no determination could be made as to the type of diesel, the purchases were taxed at 50-percent. There is no disagreement between Taxpayer and the Department on the application of the law, but rather this is a matter of Taxpayer matching up purchase documentation sufficiently to exempt use, as Taxpayer is required to maintain its records in such a fashion that the Department can determine its taxes owed. IC § 6-8.1-5-4(a).

Again, because Taxpayer has distinct businesses, the Department's audit treated purchases of equipment repair parts and tires as taxable when it could be determined that the items were used in Taxpayer's excavating business and non-taxable if the items were installed equipment being resold or on public transportation equipment. However, where no invoices were available or it could not be determined what the items were used for, the Department's auditor and Taxpayer agreed that 25-percent would be treated as used in the excavating business and therefore taxable. Again, there is no disagreement between Taxpayer and the Department on the application of the law. This is a matter of Taxpayer producing documentation sufficient to establish exempt use, as Taxpayer is required to maintain its records in such a fashion that the Department can determine its taxes owed. IC § 6-8.1-5-4(a).

For items listed on Page 11, lines 13 and 14, Page 16, line 14, Page 21, line 4, and Page 25, lines 22 through 32. Taxpayer has now provided invoices along with the monthly statements showing that a portion of the purchase was for "on road" diesel fuel and therefore exempt. The Department's supplemental audit will recalculate accordingly.

For the items listed on Page 11, lines 18 and 19, Page 16, lines 2, 3, 11, 12, and 16, and Page 25, line 19, Taxpayer now provides invoices showing that sales tax had been paid, therefore the supplemental audit will subtract those amounts from the taxable total.

For the lease of equipment listed on Page 13, lines 10 through 27, Taxpayer has presented rental agreements showing that sales tax was charged on the lease of the equipment. The supplemental audit will remove these items. Also, the equipment, which was purchased by Taxpayer tax-free, is subjected to tax on Page 17, line 1, Page 18, lines 8 and 9, Page 21, line 7, Page 25, line 1, and Page 26, lines 12, 13, and 14 (all Taxpayer's financing of the equipment). Since the equipment was purchased for resale, the supplemental audit will also remove the items on Page 17, line 1, Page 18, lines 8 and 9, Page 21, line 4, Page 25, line 1, and Page 26, lines 11, 12, 13. IC § 6-2.5-4-1.

For the item listed on Page 24, line 5, Taxpayer has provided an exemption certificate. A supplemental audit will remove this item. IC § 6-2.5-8-8(a).

For all the other items, a supplemental audit will determine if the items can be connected to non-taxable use given the new documentation presented, otherwise the charges will remain subject to tax.

Page 14, lines 1, 2, 4, 5, and 6: These items include trucks and other vehicles that the audit subjected to use tax because the audit determined that they were being used to deliver Taxpayer's own products and therefore did not qualify for the public transportation exemption. Taxpayer has presented documentation that it claims ties these vehicles to its public transportation business. A supplemental audit will review Taxpayer's documentation to ascertain whether or not this is the case.

### FINDING

Taxpayer's protest of the assessment of sales tax is denied in part and sustained in part as delineated above.

### III. Tax Administration – Negligence Penalty.

#### DISCUSSION

The Taxpayer also protested the imposition of the ten percent negligence penalty pursuant to IC § 6-8.1-10-2.1. Indiana Regulation [45 IAC 15-11-2](#)(b) clarifies the standard for the imposition of the negligence penalty as follows:

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated

as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The standard for waiving the negligence penalty is given at [45 IAC 15-11-2\(c\)](#) as follows:

The department shall waive the negligence penalty imposed under [IC 6-8.1-10-1](#) if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section. Factors which may be considered in determining reasonable cause include, but are not limited to:

- (1) the nature of the tax involved;
- (2) judicial precedents set by Indiana courts;
- (3) judicial precedents established in jurisdictions outside Indiana;
- (4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc;
- (5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

Taxpayer has not affirmatively established, as required by [45 IAC 15-11-2\(c\)](#), that its failure to pay sales and/or use tax on its sales and purchases was due to reasonable cause and not due to negligence.

#### **FINDING**

Taxpayer's protest is respectfully denied.

#### **CONCLUSION**

Taxpayer's protest of some items the Department's subjected to sales or use tax is sustained in part and denied in part. A supplemental audit will recalculate the liabilities subtracting the items on which Taxpayer has been sustained. For those items that were neither denied nor sustained, a supplemental audit will review Taxpayer's documentation to determine if Taxpayer has sufficiently tied the items to exempt use.

Taxpayer's protest of the negligence penalty is respectfully denied.

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